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Free Trade Agreements – How will they be affected by Donald Trump?

Term Paper presented by

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1. Introduction

Free trade agreements are a constantly discussed issue within economies and between relations within the whole world. Every economy is currently dealing with a lot of free trade agreements influencing their economic situation. All over the world, there are currently over 225 free trade agreements in circulation.¹

The discussions are mostly focused on the advantages and disadvantages they have on specific economies. In particular, after the last presidential campaign in the U.S. free trade agreements are discussed over and over again especially due to Donald Trump's frequent negative statements on trade agreements. Most people are sure that from January on the negotiations about the agreements will start again in another way than Barack Obama ended with them.

The question is how, in what dimension, the situation with free trade agreements will change under Donald Trump and therefore what effects the presidential election has on the U.S. economy. Furthermore, people wonder what Donald Trump will initiate instead.

But one has to have in mind that not only Donald Trump could be the responsible for slowing down trade in the future, trade deals are already decreasing without him. This is shown by the fact that over the past few years the numbers changed.² The volume of world trade increased only about 3% a year since 2012 which means "less than half the average expansion rate over the prior three decades" (Bloomberg Businessweek, 2016, p.16).²

To understand possible consequences of Donald Trump's approach, it is first necessary to know about some fundamental facts about the meaning of trade for the U.S. economy over the past decades until now.

¹ Reed, R, Lira, C, Lee, B, & Lee, J 2016, 'Free Trade Agreements and Foreign Direct Investment: The Role of Endogeneity and Dynamics', *Southern Economic Journal*, 83, 1, p. 176

² Einhorn, B, Brautlecht, N, & Roberts, D 2016, 'Global Trade Is Slowing', *Bloomberg Businessweek*, 4500, p. 16

2. The U.S. and Trade

Trade is an important part of the American economy since years. In general, people are convinced that trade has positive effects for the U.S. economy and should therefore be maintained. To avoid trade agreements with other economies would end in negative effects for the economic situation of the U.S. as a withdrawal of specific agreements would show a political and economic distance to these countries which is definitely not supporting global relationships.³

2.1 The U.S. History with Trade

The U.S. economies' discussions about trade have its origin in the American history and are part of it since the early nineteenth century. At that time, the country's objectives were divided into those of the northern manufacturers and those of the southern manufacturers. While the northern manufacturers wanted to achieve the setting of high tariffs on rival importing products, southern manufacturers supported free trade deals to encourage their exports to other countries to gain the most possible profit. Over the years, the majority had a tendency towards higher tariffs which changed a few years later to the opposite, to lower tariffs. Cordell Hull, who held the office of the Secretary of the State at that time, wanted to hold low tariffs but he was worried about the Congress bringing them down at that time, future Congresses let them increase later again. Due to the objective of the implementation of low tariffs, Cordell Hull started negotiating trade agreements with other economies. The target was to decline U.S. tariffs in exchange of others economies decreasing theirs which was successfully confirmed by the Congress. The results of these negotiations generated a trade surplus of the goods fabricated within the country.⁴

³ Irwin, DA 2016, 'The Truth About Trade', *Foreign Affairs*, 95, 4, pp. 84-85

⁴ Destler, IM 2016, 'America's Uneasy History with Free Trade', *Harvard Business Review Digital Articles*, pp. 2-3

Till the “GATT”, which describes the “General Agreement on Tariffs and Trade” and was established after World War II, the trade agreements of the U.S. economy were reduced to only bilateral agreements. The “GATT” agreement pursued the target to further on reduce trade barriers and resulted in the fall of U.S. tariff rates from 60% in 1930 to 5.7% in 1980 and to 2.7% in 2013. These developments helped creating the American, as well as foreign markets for global and international trade relationships.⁵

2.2 Free Trade Agreements

Till the 1980s, most of the free trade agreements of the U.S. were reduced to agreements with only a few economies. The relationship of the U.S. economy with Canada was a special one, as they were “each other’s largest trading partner” (Harvard Business Review Digital Articles, 2016, p. 4).⁶ Therefore, around the 1980s, Canada tried to create a bilateral trade agreement with Washington to force this relationship which was accepted by the Congress in 1988. The U.S. also liked to force its trade relationships with Europe which was partially prevented by their resistance. Concerning to this, the U.S. hoped that their trade agreements with Canada caused Europe to also agree to the creation of trade relationships with the American economy. The agreement between Canada and the U.S. was the trigger for Mexico to also create a trade relationship with the U.S. whereby the establishment of the North American Free Trade Agreement (NAFTA) took place and was accepted in 1993, even though it was first discussed due to the risks it created for U.S. jobs. Because wages in Mexico are much less than the American ones. This led to benefits for the Mexican population and their products. At that time, the creation of free trade agreements all over the world integrated as a very important part of the U.S. policy. But at some point, the focus, especially during the presidential period of George W. Bush, lied on bilateral agreements.⁶

⁵ Destler, IM 2016, 'America's Uneasy History with Free Trade', *Harvard Business Review Digital Articles*, p. 3

⁶ Ibid., p. 4

Nowadays, free trade agreements between economies are important for a global market development and show positive effects for each country's economy. Trade deals particularly are important for decreasing tariffs, price reductions and a diversity and improvement in goods imported. At this point, the Transatlantic Trade and Investment Partnership (TTIP) can be mentioned as a free trade agreement between the U.S. and the European Union and is negotiated since June 2013. The negotiations were planned to be finished by the end of 2016.⁷

A further free trade agreement is the Trans-Pacific Partnership (TPP), which was declared in October 2015 and represents a trade deal between the U.S. and 11 other economies which include: Japan, Malaysia, Vietnam, Singapore, Brunei, Australia, New Zealand, Canada, Mexico, Chile and Peru. The main objective of this agreement for the American country was to reduce tariffs on goods produced in the U.S.⁸

To understand the importance of these free trade agreements some numbers are mentioned: "The TPP economies represent 27.3% of world GDP and 10.7% of the world's population. The TTIP economies represent 33% of world GDP and 11.2% of the population. The average income per capita for the 12 TPP countries is \$30,697, while the TTIP average income is \$47,607." (Marketing News, 2016, p. 2).⁷

2.3 Barack Obama and Trade

When Barack Obama started his first presidential period, he was not a real supporter of trade agreements but this changed to the opposite during his second period. He particularly supported the Trans-Pacific Partnership (TPP) as in his opinion this agreement was not only necessary for the U.S. economy but also for the international economic development. A further step for him was to establish the Transatlantic Trade

⁷ 'New Rules of Engagement: Understanding TTIP and TTP' 2016, *Marketing News*, 50, 7, pp. 1-2

⁸ DuPuis, R 2016, 'How will Trump's trade, tariff policies affect manufacturing?', *Central Penn Business Journal*, 32, 47, p. 6

and Investment Partnership (TTIP) to force trade relationships with Europe.⁹ If all his effort for these agreements was for nothing is not clear until the economy experiences the ongoing procedure under Donald Trump.

2.4 Free Trade and the U.S. Economy and Manufacturers

The Great Recession in the U.S., which took place between 2007 and 2009, brought critical times for most of the American workers. People are suffering until these days from losing their jobs, staying unemployed and receiving only low wages as around nine million jobs were lost due to this recession. Especially these workers are convinced that trade agreements only lead to even more job losses and lower wages. That is why for example many workers once voted for a campaign against the North American Free Trade Agreement (NAFTA). In general, workers and manufacturers are persuaded that imports from foreign countries are the main reason for job losses but that is not the only aspect. Another factor which only few people have in mind is the more and more developing technology. Technology develops automation, productivity and efficiency and leads therefore to the need of less workers.¹⁰ This is proved by a study of the Center for Business and Economic Research at Ball State University. This study showed that “productivity growth accounted for more than 85% of the job loss in manufacturing” while “just 13% of the overall job loss resulted from trade” (Foreign Affairs, 2016, p. 88).¹⁰

That is why American manufacturers are the ones that focus most on the development of the free trade agreements under Donald Trump. Some manufacturers fear that with the trade discussions also issues like “tax reform, workforce, regulations, etc.” get renegotiated which could be “negatively impacting the economy and manufacturing”. Therefore, according to the U.S. manufacturers, the focus should lie on “policies that make it easier for manufacturing in the U.S.” (DuPuis, R 2016, 'How will Trump's

⁹ Destler, IM 2016, 'America's Uneasy History with Free Trade', *Harvard Business Review Digital Articles*, p. 5

¹⁰ Irwin, DA 2016, 'The Truth About Trade', *Foreign Affairs*, 95, 4, pp. 87-89

trade, tariff policies affect manufacturing?', *Central Penn Business Journal*, 32, 47, pp. 7).

The questions is what do experts think? On the one hand, most of the economist are convinced that trade is in general an economic advantage for each country that deals with trade. On the other hand, critics say that trade deals are the reason for putting “the U.S. and its manufacturing workers in a race to the bottom” (Newsweek Global, 2016, p. 14)¹¹ and make them responsible for most of the job losses in manufacturing. An example for this negative impact of trade deals is the North American Free Trade Agreement (NAFTA). There are companies having their factory in the U.S. but who close it and move to Mexico which is working in an easy way due to the trade agreement. As a result, U.S. workforce loses their jobs as the U.S. companies prefer the lower wages they have to pay in Mexico.¹¹ Due to actions like these, “NAFTA-related job losses in the U.S. ranged from 60,000 to 190,000” (Newsweek Global, 2016, p. 14).¹¹

These numbers also relate to a statistic from the labor-backed Economic Policy Institute that says that “NAFTA costs the U.S. 700,000 jobs over 20 years”. This number sounds big but on the other side the NAFTA deal brings “economic growth and trade flows” which influence the economy positively (Matthews, C 2016, 'The Tide that sinks all Boats', *Fortune*, 174, 4, p. 14).

¹¹ Powell, B 2016, 'Are Free Trade Deals bad for America?', *Newsweek Global*, 166, 24, pp. 12-14

3. Donald Trump and Trade

As experienced due to the last presidential election campaign, people know that Donald Trump, the next president of the United States of America, is not a real supporter of the free trade agreements the U.S. economy is currently dealing with.

Before Donald Trump was elected, he already criticized the agreements and said that “if elected, he’ll abandon talks on the 12-nation Trans-Pacific Partnership” and that he plans to “renegotiate the 1993 North American Free Trade Agreement” as these trade deals are the reason for “poverty and heartache” in the country according to him (Bloomberg Businessweek, 2016, p. 20).¹² He represents the opinion trade agreements like the Trans-Pacific Partnership reduce the American independence.¹²

There are three points he most focuses on. Firstly, in his opinion, globalization is the trigger for dividing the population into the “financial elite” (Logistics Management, 2016, p. 18)¹³ which gets wealthier and the numerous workers falling into poverty. Secondly, he is convinced that the most free trade agreements are having negative impacts for the American economy. According to Donald Trump, the better way are bilateral trade agreements. Thirdly, Donald Trump sees a big problem in the Chinese economy. He sees China as a “currency manipulator” (Logistics Management, 2016, p. 18)¹³ and would therefore set tariffs on exports from China.¹³

Donald Trump takes the view that China is setting down the value of their currency to rise their exports which results in benefits in trade for the Chinese economy and is in his opinion therefore an act of unfair trade dealing.¹⁴

¹² Greeley, B 2016, 'Trump Has One Approach to Trade', *Bloomberg Businessweek*, 4482, pp. 20-21

¹³ Berman, J 2016, 'Trump's proposed trade policies won't be embraced by all, says Panjiva', *Logistics Management*, 55, 8, p. 18

¹⁴ Einhorn, B, Brautlecht, N, & Roberts, D 2016, 'Global Trade Is Slowing', *Bloomberg Businessweek*, 4500, p. 17

A further problem with the Chinese economy for the U.S. is the fact that due to their domestic economic growth, China wants to retract from exporting economies as they are able to use their own resources for manufacturing. This step might seem great for the Chinese economy but with regard to global trade this declines trade actions.¹⁵

Especially for the U.S., that always exported a lot of materials to China, this is a risk for the American economy. But not only China is a threat for Donald Trump, also Mexico. Due to importing products from Mexico, Donald Trump wants to set tariffs on their goods.

As Donald Trump always talks about the protection of the American population as one of his main objectives, of course he criticizes imports from other countries as these goods could easily be manufactured in the home country.¹⁶ If the products are developed in other countries, this could mean the loss of jobs for U.S. workers and manufacturers, but at the same time, producing in foreign countries is sometimes cheaper than producing at home. Therefore the location of manufacturing the goods is always a controversial issue.

3.1 Renegotiations

Donald Trump underlines that he is not a complete opponent of trade deals, quite the contrary, “he’s a free trader at heart” (Bloomberg Businessweek, 2016, p. 20)¹⁷ but his objective is to renegotiate the existing deals of the U.S. trade policy to make sure that better and fairer deals are developed which over all secure the American population as free trade deals have shown bad times in the past for some Americans. Donald Trump is convinced that some trade deals are damaging American manufacturers.¹⁷

¹⁵ Einhorn, B, Brautlecht, N, & Roberts, D 2016, 'Global Trade Is Slowing', *Bloomberg Businessweek*, 4500, p. 17

¹⁶ Kuehl, C 2016, 'Politicized Stances on Transportation, Trade Could Hurt Industries Like Shipping Throughout 2016 and Beyond', *Business Credit*, 118, 7, p. 11

¹⁷ Greeley, B 2016, 'Trump Has One Approach to Trade', *Bloomberg Businessweek*, 4482, p. 20-21

His idea of the protection of the American population and manufacturers include, over all, the setting of high tariffs on imported goods and the stopping the loss of jobs¹⁸ which in his opinion mostly result from free trade agreements. Donald Trump even calls the Trans-Pacific Partnership (TPP) “a rape of our country” (Matthews, C 2016, 'The Tide that sinks all Boats', *Fortune*, 174, 4, p. 13).

3.2 Bilateral Trade

According to Donald Trump’s statements, especially during the election campaign, people know that he favors bilateral trade deals instead of free trade agreements with more than one or two countries. One need to know, that these deals would definitely work for the American economy, as the U.S. is a very big country. No matter with which county the U.S. would deal, it’s obvious that the U.S. would be the bigger one and would therefore always “win more than it gives away” (Logistics Management, 2016, p. 18).¹⁹ Donald Trump sees the benefits not only in the administrative fact that bilateral trade agreements are much easier to handle but even more in economic issues.¹⁹

3.3 Possible Consequences through Trump’s Changes

To completely abandon the existing free trade agreements could have negative impacts on the U.S.

According to Donald Trump, the North American Free Trade Agreement (NAFTA) for example only leads to negative consequences for the U.S. workers and manufacturers, but at the same time, in the past few years, it led to positive developments for the Mexican economy. Of course, this is definitely not Trump’s objective, as he again and again mentioned his negative and at some point racist opinion about that the Mexicans

¹⁸ DuPuis, R 2016, 'How will Trump's trade, tariff policies affect manufacturing?', *Central Penn Business Journal*, 32, 47, p. 6

¹⁹ Berman, J 2016, 'Trump's proposed trade policies won't be embraced by all, says Panjiva', *Logistics Management*, 55, 8, p. 18

should be brought out of the American country. But over the past few years, due to the NAFTA, the Mexican demand for products of the U.S. raised heavily²⁰ and “more Mexicans have left the United States than have come in” (Foreign Affairs, 2016, p. 93-94)²⁰ which should be a significant aspects for Donald. So why should he renegotiate or even abandon this agreement? The consequences would result in the exact way he tries to avoid regarding to the situation with the Mexican population. This step would not make any sense according to his prior statements.

The U.S. needs trade agreements to promote exports. Without any trade agreements, foreign markets would not be that present for the U.S. than they are with them. This point is even more important than the opening of the U.S. market to receive foreign imports.²¹ Therefore, the U.S. economy would maybe receive the same amount of imports but wouldn't be able to export the amount they are exporting currently. This would of course result in a big trade deficit for the whole economy.

A further aspect of negative consequences is that if the U.S. would escape from many of their trade agreements of course the whole world would not do the same. The rest of the world would keep negotiating trade agreements with other countries. This would only result in the U.S. exporters losing competition benefits in comparison with the rest of the world.²²

²⁰ Irwin, DA 2016, 'The Truth About Trade', *Foreign Affairs*, 95, 4, pp. 93-94

²¹ Ibid., p. 93

²² Ibid., p. 94

4. Conclusion

It is definitely correct, that some of what Donald Trump says about the effects of trade on the American population, especially the manufacturers, correspond to the truth, “but if he wants both trade and trade reform, he’s going to need more than just a better deal” (Bloomberg Businessweek, 2016, p. 21).²³ It is of great importance that Donald Trump needs to stop thinking negotiating about political issues is the same as acting like a businessman where it is said that one part is winning and one is losing. Normally, there is not a winner and a loser, in general every part of a trade agreement carries away advantages.²⁴ That means trade is part of each economy and is always “a two-way street – the exchange of exports for imports” (Foreign Affairs, 2016, p. 85).²⁴

Furthermore, it is obvious, that “some of what Trump proposes is within the president’s power, but not all” (DuPuis, R 2016, 'How will Trump's trade, tariff policies affect manufacturing?', *Central Penn Business Journal*, 32, 47, p. 6). That means, his objectives could not be reached that easy. His action would maybe result in reactions of the U.S. trading partners. Furthermore, there exists no safe prove that Donald Trump’s plans and objective will be putted into practice successfully.²³

No matter what kind of trade agreements exist now or in the future and however they will change under Donald Trump, as the European Commission Vice President Jyrki Katainen said: “Free trade must be fair, and only fair trade can be free” (Einhorn, B, Brautlecht, N, & Roberts, D 2016, 'Global Trade Is Slowing', *Bloomberg Businessweek*, 4500, p. 16).

One statement of Hillary Clinton also underlines the importance of trade for the U.S. economy: “We are 5% of the world’s population, we have to trade with the other 95% (Matthews, C 2016, 'The Tide that sinks all Boats', *Fortune*, 174, 4, p. 14).

How the situation with the free trade agreements will really develop in the future is at the earliest to see from January on.

²³ Greeley, B 2016, 'Trump Has One Approach to Trade', *Bloomberg Businessweek*, 4482, p. 21

²⁴ Irwin, DA 2016, 'The Truth About Trade', *Foreign Affairs*, 95, 4, p. 85

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